

Message Text

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C O N F I D E N T I A L MADRID 1146

LIMDIS

E.O. 11652: GDS
TAGS: EFIN, ECON, SP
SUBJECT: VIEWS OF BANK OF SPAIN RESEARCH DIRECTOR ANGEL ROJO
ON THE SPANISH ECONOMY; ANNUAL IMF CONSULTATIONS VISIT

1. SUMMARY: BANK OF SPAIN RESEARCH DIRECTOR ROJO STRONGLY BELIEVES THE GOS SHOULD HAVE UNDERTAKEN AN ECONOMIC STABILIZATION EFFORT IMMEDIATELY AFTER ITS SUCCESS IN THE REFERENDUM ON POLITICAL REFORM. HE STILL BELIEVES THAT IT SHOULD ACT BEFORE ELECTIONS, CONTRARY TO THE APPARENT PREVAILING VIEW IN THE GOVERNMENT, HE THINKS IT WILL NOT BE IN AS GOOD A POSITION POLITICALLY TO ACT AFTER ELECTIONS. ONE POSSIBLE MEANS OF INFLUENCING THE GOVERNMENT IS THROUGH THE IMF ANNUAL CONSULTATIONS MISSION SCHEDULED TO BE IN MADRID FOR TWO WEEKS BEGINNING FEBRUARY 16. ROJO'S INFORMATION ON THE ECONOMY CONFORMS ROUGHLY TO THAT TRANSMITTED IN THE EMBASSY'S TELEGRAM 1145 EXCEPT THAT MOST RECENT DATA INDICATE THAT 1976 FISCAL PERFORMANCE TURNED OUT CONSIDERABLY BETTER THAN HAD BEEN EXPECTED. END SUMMARY.

2. ANGEL ROJO DUQUE IS ONE OF SPAIN'S MOST PRESTIGIOUS ECONOMISTS AS WELL AS DIRECTOR OF RESEARCH FOR THE BANK OF SPAIN. HE GAVE THE DCM THE FOLLOWING FRANK VIEWS ON
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THE STATE OF THE ECONOMY ON FEBRUARY 10.

3. HE HAD BEEN ONE OF THOSE WHO THOUGHT THAT THE GOVERNMENT SHOULD NOT ATTEMPT A STABILIZATION PROGRAM BEFORE IT HAD ESTABLISHED ITSELF POLITICALLY THROUGH THE REFERENDUM. BUT THE RESULTS OF THE REFERENDUM HAD PLACED IT IN A VERY STRONG POSITION POLITICALLY, AND IT SHOULD HAVE ACTED

IMMEDIATELY THEREAFTER. IT STILL SHOULD ACT BEFORE ELECTIONS. IN FACT, THERE WAS A REAL POSSIBILITY THAT PUBLIC KNOWLEDGE OF THE SERIOUSNESS OF THE ECONOMIC SITUATION AND OF THE INEVITABILITY OF EVENTUAL SUBSTANTIAL DEVALUATION WAS REACHING A POINT THAT THE GOVERNMENT WOULD BE FORCED TO TAKE SOME SORT OF MAJOR ACTION BEFORE ELECTIONS DESPITE ITS EVIDENT CURRENT INTENTION TO AVOID THIS. (ROJO WAS CLEAR THAT HE WAS NOT PRIVY TO THE GOVERNMENT'S PLANS, BUT DID NOT THINK IT HAD ANY PRESENT INTENTION TO TAKE DECISIVE ACTION BEFORE ELECTIONS.) THERE WAS NO REASON TO BELIEVE THE GOVERNMENT'S POLITICAL POSITION WOULD BE STRONGER OR THAT THE GOS WOULD HAVE MORE VALID INTERLOCUTORS AFTER ELECTIONS. IN FACT, IF THE CONSERVATIVES AND THE CENTER SWEEPED THE BOARDS IN THE ELECTIONS AND THE LEFT DID POORLY, THE LEFT MIGHT THEN FEEL IT MUST BE ALL THAT MORE INTRANSIGENT WITH RESPECT TO THE NEEDED STABILIZATION PROGRAM.

4. ALTHOUGH FINAL 1976 BALANCE OF PAYMENTS DATA WERE NOT YET AVAILABLE, IT APPEARED THAT THE CURRENT ACCOUNT DEFICIT WAS BETWEEN \$4.2 AND \$4.3 BILLION. TOTAL FOREIGN EXCHANGE RESERVES WERE DRAWN DOWN BY ABOUT \$1 BILLION AND FOREIGN DEBT INCREASED BY ABOUT \$3 BILLION TO AROUND \$12 BILLION. FOREIGN INVESTMENT WAS DRYING UP. THE PUBLIC WAS INCREASINGLY EXPECTING A DEVALUATION AND THIS WAS AFFECTING FINANCIAL ARRANGEMENTS IN MULTIPLE WAYS, INCLUDING LEADS AND LAGS, ADVERSE TO THE 1977 BALANCE OF PAYMENTS PROSPECTS. FOREIGN COMMERCIAL BANKERS WERE BECOMING MORE INSISTENT IN THEIR QUERIES ABOUT THE PROSPECTS AND INCREASINGLY UNLIKELY TO EXTEND LARGE ADDITIONAL CREDITS WITHOUT A REASONABLE
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GOS FINANCIAL PROGRAM. HE WAS PERSONALLY DUBIOUS ABOUT THE PROSPECTS FOR ARAB COUNTRY LOANS THAT WOULD MAKE MORE THAN A SHORT-TERM DIFFERENCE IN THE SITUATION.

5. ROJO DISPUTED ARGUMENTS THAT OFFICIAL DATA INDICATING A 20 PERCENT INCREASE IN THE COST OF LIVING IN 1976 WERE EXAGGERATED. HE ALSO CONFIRMED THAT PRESENT POLICY CONTEMPLATES EXPANSION OF MONEY SUPPLY IN 1977 AT A 21 PERCENT ANNUAL RATE, ALTHOUGH HE IMPLIED THAT THE ISSUE HAD NOT YET BEEN SYSTEMATICALLY DISCUSSED WITHIN THE GOVERNMENT. HE FURTHER SAID THAT WAGE NEGOTIATIONS WERE LEADING TO CONSTRUCTION WAGE INCREASES OF MORE THAN 30 PERCENT AND OTHER WAGE INCREASES OF BETWEEN 25 AND 30 PERCENT. HIS PERSONAL VIEW WAS THAT THE GOVERNMENT SHOULD ADOPT A MONEY SUPPLY ANNUAL GROWTH TARGET FOR 1977 OF AROUND 15 PERCENT WHICH, INTER ALIA, WOULD CAUSE BUSINESS TO BE MORE HARD-NOSED IN ITS WAGE NEGOTIATIONS AND WORKERS IN TURN TO UNDERSTAND THAT INSISTING ON TOO MUCH MIGHT REALLY COST THEM JOBS.

6. THE ONE BRIGHT SPOT IN THE PICTURE, ACCORDING TO ROJO, WAS THAT SURPRISINGLY THE PUBLIC SECTOR, COMPOSED OF THE CENTRAL AND LOCAL GOVERNMENTS, SEMI-AUTONOMOUS AGENCIES (INCLUDING SOCIAL SECURITY AGENCIES AND FORPA) AND NET PUBLIC CREDIT, HAD TURNED OUT TO BE ROUGHLY IN BALANCE INSTEAD OF SOME 100 BILLION PESETAS IN DEFICIT AS ESTIMATED BY THE MINISTER OF FINANCE AT THE END OF DECEMBER. THE EXPLANATION SEEMED TO BE PRINCIPALLY THAT THE GOVERNMENT AGENCIES HAD NOT SPENT AS MUCH AS EXPECTED. NO ONE YET KNEW WHAT EFFECT THIS PHENOMENON WOULD HAVE ON FISCAL PROSPECTS FOR 1977. (WE WILL BE LOOKING INTO THIS NEW DEVELOPMENT. ROJO'S OWN STAFF USED THE 100 BILLION FIGURE WITH US TWO WEEKS AGO. ONE POSSIBILITY IS THAT PART OF THE ANTICIPATED DEFICIT HAS BEEN COVERED BY FOREIGN BORROWING.)

7. ROJO CONFIRMED THAT HE, FUENTES QUINTANA, LASUEN, AND TWO OR THREE OTHERS, HAD BEEN ASKED BY PRIME MINISTER SUAREZ TO BE ECONOMIC ADVISORS TO HIM WITH VOICE BUT NOT CONFIDENTIAL

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VOTE IN GOVERNMENT COUNCILS, SHORTLY AFTER SUAREZ TOOK OFFICE. HE HAD TURNED THE PROPOSITION DOWN BECAUSE HE FELT HE WOULD HAVE HAD TO LEAVE THE BANK OF SPAIN TO ACCEPT IT AND ALSO BECAUSE HE WAS NOT SURE AT THAT TIME THAT SUAREZ WOULD BE A LIBERALIZER POLITICALLY. THE REST OF THOSE ASKED HAD ALSO BEEN UNWILLING TO SERVE FOR A VARIETY OF THEIR OWN REASONS. THEREAFTER, FOR A TIME, MINISTER OF INDUSTRY PEREZ DE BRICIO HAD SEEMED TO HAVE A VERY STRONG VOICE IN ECONOMIC POLICY. MORE RECENTLY, THE PLANNING STAFF OF THE PRESIDENCY UNDER RICARDO CALLE SEEMED TO HAVE GROWN IN INFLUENCE. MINISTER OF FINANCE CARRILES WAS TOO INDECISIVE TO BE VERY INFLUENTIAL, AND THE BANK OF SPAIN, IN SPITE OF CURRENT GOVERNOR LOPEZ DE LETONA'S REPUTED CLOSE RELATIONSHIP WITH THE KING, WAS BEING CALLED ON VERY LITTLE FOR ADVICE. ROJO HAD HOPED THAT THE REGULAR ANNUAL INTERNATIONAL MONETARY FUND CONSULTATIONS MISSION, DUE TO BEGIN A TWO WEEKS' VISIT ON FEBRUARY 16, MIGHT HAVE AN IMPACT. BUT AT THIS POINT, HE WAS NOT EVEN SURE THAT THE MINISTER OF FINANCE WOULD SPEND TIME WITH IT, AND HE WAS CERTAIN THAT ITS INFLUENCE WOULD BE MINIMAL UNLESS THE PRESIDENCY COULD IN SOME WAY BE INTERESTED IN ITS FINDINGS.

8. COMMENT: EMBASSY OFFICERS ARE SCHEDULED TO LUNCH NEXT WEEK WITH PRESIDENCY SECRETARY FOR PLANNING RICARDO CALLE AND MEMBERS OF HIS STAFF. AT THAT TIME, AS WELL AS OBTAINING CALLE'S VIEW OF THE CURRENT SITUATION AND FUTURE PROSPECTS, THEY WILL SUGGEST THAT HE, AND PERHAPS OTHER ELEMENTS OF THE PRESIDENCY, BE IN CONTACT WITH THE FUND MISSION IF SUCH CONTACT IS NOT ALREADY CONTEMPLATED. STABLER

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